SUPREME COURT, U. S.
APR 20 1967
JOHN F. DAVIS, CLE

IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

No. ~~1289~~ 96

JERSEY STATE BANK, *Petitioner*

v.

ROYAL INDEMNITY COMPANY

and

THE UNITED STATES, *Respondents*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

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The Petitioner prays for a Writ of Certiorari to review the judgment of the United States Court of Claims in this case.

OPINION BELOW

The opinion of the Court of Claims is reported at Appendix A, infra, pp. 1a to 6a.

JURISDICTION

The opinion of the Court of Claims was entered January 20, 1967. The jurisdiction of this Court is invoked under Section 28 U.S.C. 1255 (1).

QUESTIONS PRESENTED

1. Whether a Government Contractor's assignee, which loaned money to the Contractor for the performance of the Contract, under an assignment pursuant to the Assignment of Claims of 1940, as amended, has a superior equity to that of a surety which made payments to creditors under a payment bond?

2. Whether or not this Court should distinguish from its previous decisions and decide that in payment bond cases the assignee bank has a prior claim?

STATUTES INVOLVED

The pertinent portions of the Assignment of Claims Act of 1940, 54 Stat. 1029, 31 U.S.C. Sec. 203; as amended by the Act of May 15, 1951, 65 Stat. 41; (41 U.S.C. Sec. 15) are set forth in Appendix A, infra; p. 6a.

Miller Act, 49 Stat. 793, 40 U.S.C. Sec. 270(a), set out in Appendix A, infra, p. 9a.

STATEMENT

Petitioner, Jersey State Bank, (Hereinafter called the Assignee Bank) seeks the sum of $31,200.00 plus interest thereon, out of the total sum of $38,461.20 being held by the United States in retainages. The plaintiff below, Royal Indemnity Company (hereinafter called the Surety) claims the total balance of $38,461.29 held by the Government in accordance with its surety con-

tract with Albert M. Barbato (hereinafter called the Contractor). The United States admits that it holds $38,461.29 but seeks a set-off of $2,213.07, plus interest for withholding taxes not paid by the Contractor and considers itself a stakeholder for the balance.

On May 31, 1963, the Contractor, as collateral for loans agreed to be made by the Assignee Bank for the performance of the contract, assigned any and all sums of money then due or "to become due" from the United States Government by virtue of its contract with the Contractor. The said assignment was made pursuant to the provisions of the Assignment of Claims Act of 1940, as amended, P.L. 30, May 15, 1951, 65 Stat. 41; 31 U.S.C. Sec. 203; 41 U.S.C. Sec. 15; and as required by said Act, the Assignee Bank gave proper notice to the Contracting Officer, the Disbursing Officer and the Surety, of such assignment.

Prior to the execution of the contract, on April 12, 1963, the Contractor, as principal, and Royal Indemnity Company, as surety, executed a performance bond as required by the Miller Act, 39 Stat. 793, 40 U.S.C. Sec. 270(a). Also executed were labor and material payment bond under the said Miller Act, conditioned upon the payment by the Contractor, as principal, of all persons supplying labor and material in the prosecution of the work called for by the Contract.

During September of 1964, the Government discovered that the Contractor, having completed approximately ninety-eight (98%) per cent of the work, was unable to complete the remainder. Accordingly, an informal agreement was made to accept the work in its then condition and to delete the uncompleted items from the Contract by the issuance of a Change Order. In accordance with this informal agreement, the con-

tract was amended to delete the remaining work and to reduce the contract price by $12,300.00. As so amended, the contract work was accepted as completed and the contractor discharged. At no time was the Contractor held to be in default. The unpaid balance of the contract price upon completion in the manner aforesaid totaled $38,461.29.

Surety alleges that it paid the sum of $220,470.00 to the creditors of the Contractor in settlement of their claims for labor and materials on the Contract, none of which has been refunded or paid to the Surety by the Contractor or any other person, and accepted assignment of their claims against the Contractor. Accordingly, the Surety has claimed herein the balance due the Contractor by the Government.

REASONS FOR GRANTING THE WRIT

The reasons for granting the Writ of Certiorari follow:

1. Neither the United States Court of Claims nor this Honorable Court have, in prior cases, given full consideration to the impact of the Assignment of Claims Act of 1940, as amended. The provisions of the said Assignment of Claims Act are meaningless, unless that Act is interpreted to accord to a bank or other financial institution making loans to a Government Contractor, secured by an Assignment of the funds due or to become due under the contract, or an absolute right to the contract fund unless or until the contract is terminated for the default of the Contractor. A distinction is here made between a payment bond and a performance bond.

Even an assignee would have to concede this because the termination of the contract for default cuts off the

assignee's rights and forces the surety either to complete the defaulted work under the Performance Bond, or to pay the excess if the Government completes it by re-letting.

However, absent a default and the concomitant Government rights to complete the performance of the Contract and hold Contractor and surety under the Performance Bond, the assignment is unaffected, and the United States, which by statute has recognized the assignment as absolutely valid, must recognize it.

Under the provisions of the Miller Act, Act of August 24, 1935, 49 Stat. 793, 40 U.S.C. Sec. 207(a), every Contractor, before he may be awarded a Contract exceeding $2,000.00 in amount, for the construction, alteration or repair of any public building or public work of the United States, is required to furnish (1) a Performance Bond with a surety or sureties satisfactory to the Contracting Officer and in such amount as he shall deem adequate for the protection of the United States; and (2) a Payment Bond, with a surety or sureties satisfactory to the Contracting Officer for the protection of all persons supplying labor and material in the prosecution of the work provided for in said Contract for the use of each such person.

Prior to the Assignment of Claims Act of 1940, sureties who furnished the Performance and Payment Bonds required by the Act, were thus prohibited from obtaining a valid assignment from the Contractor of the monies due or to become due under the Contract. After the enactment of the Assignment of Claims Act of 1940, this prohibition continued, as a surety company could not qualify, under the Act, as a bank, trust company or other financing institution. However, prior

to 1935, this Court generally recognized that a surety, who after default of a contractor was required to complete the contract under the Performance Bond, or who, after a default of the contractor was required to pay suppliers of labor and material, was entitled to be subrogated to the rights of the United States Government. Such right took priority, it was held, over the naked claim of an assignee bank, also claiming subrogation.

In the case of *Prairie State Bank* v. *United States*, 164 U.S. 27, 17 S. Ct. 142, 41 L. Ed. 412 (1896), a surety had been compelled to complete a Government contract upon the contractor's default in performance, and claimed reimbursement for his expenditures out of the retained percentage of ten (10%) per cent of the estimated value of the work done under the terms of the Contract between the original Contractor and the Government. The Prairie State Bank, contesting the surety's claim, asserted that it had a superior equitable lien arising from monies advanced by the bank to the Contractor before the surety began to complete the work. This Court recognizing that neither party could hold a valid assignment held that the Fund tended to protect the surety, and that its creation raised an equity in the surety's favor; that the United States was entitled to protect itself out of the fund; and that the surety had an equitable right of subrogation by resort to the same securities and the same remedies which had been available to the United States for its protection against the Contractor. No evidence was adduced indicating that the proceeds of the loan had been used in the performance of the contract.

In this respect, the Prairie State Bank case undoubtedly followed an already established doctrine that a

surety who completes a contract has an "equitable right" to indemnification out of a retained fund. *Hurwitz* v. *Pink,* 96 F. 2d 605; *Ward* v. *First National Bank,* 76 F. 2d 256; *New York Title & Mortgage Company* v. *First National Bank,* 51 F. 2d 485, cert. denied, 52 S. Ct. 131, 284 U.S. 676, 76 L. Ed. 572. This right however, is not a legal right. *Dedmond's Estate,* 121 P. 2d 466, 468, 170 Ore. 692; *Jasper School District* v. *Gormley,* 193 S.E. 248, 184 Ga. 756, 196 S.E. 232, 57 Ga. App. 537.

Following the *Prairie State Bank* case, this Court has decided in favor of the surety over the assignee, holding essentially that the rights of a surety were superior to the rights of an assignee of the contractors. See *Henningsen* v. *United States Fidelity & Guaranty,* 208 U.S. 404 (1908); *Hardaway* v. *National Surety Company,* 211 U.S. 552 (1909). *Martin* v. *National Surety Company,* 300 U.S. 588.

In *Pearlman* v. *Reliance Insurance Company,* 371 U.S. 132 this Court confirmed its prior decisions and held that the Surety had a prior equity. However, the question of the effect of the Assignment of Claims Act of 1940, *supra,* was not involved in that case and the Court did not consider it.

Petitioner, the Assignee Bank herein, respectfully submits that this Court has ignored the true purpose and effect of the Assignment of Claims Act of 1940, *supra,* as amended, in reaching its prior decisions. Said Assignment of Claims Act states "Notwithstanding any law to the contrary governing the validity of assignments, any assignment pursuant to this section shall constitute a valid assignment *for all purposes*" (emphasis added). Full meaning should be given this section of the Act.

CONCLUSION

For the reasons set forth above a Writ of Certiorari should be granted in order that the rights of an Assignee Bank could be determined considering the provisions of the Assignment of Claims Act.

Respectfully submitted,

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